



## 3.22.2010 Audit Committee Meeting Minutes

**To:** Kristi Tomey, Audit Committee Chairman

**From:** Chris Compton, Secretary

**CC:** Sterling Cheatham  
Debra Mack  
Allison Collins  
Stephanie Jacobs  
Bryon Dorey

**Date:** March 22, 2010

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### Call to order:

Kristi Tomey, Audit Committee Chairman, brought the meeting to order at 11:40 am on March 22, 2010 in the City Manager's Conference Room.

### Members Present:

Kristi Tomey  
Earl Sheridan  
Charlie Rivenbark

### Staff Present:

Sterling Cheatham  
Chris Compton

Allison Collins  
Debra Mack

### Summary of Action Items:

#### 1. Review for Approval – Finance Department's Loan Division Internal Audit Report – Released February 22, 2010.

- Allison Collins gave a background and chronology of events relating to the report. Areas for improvement are shown on page 15 of the report.
- Debra Mack provided background for transitioning to the new loan review procedure module.
- The goal is to be fully implemented with the new loan module procedure by June 30, 2010. The transition will include parallel testing to ensure that data is transferred accurately and complete.
- Kristi Tomey shared a concern about changing all passwords to a period of 90 days, which is the industry standard. Allison Collins and Sterling Cheatham will advise the City IT department to implement this standard city-wide.

- A motion was made by Earl Sheridan and seconded by Charlie Rivenbark to approve the Finance Department's Loan Division Internal Audit Report – Released February 22, 2010. The motion carried.

**2. Review for Approval – The recommendation to award a contract to Bank of America for the City's commercial banking services for a term of five years.**

- Debra Mack reviewed the City's background and relationship with Bank of America since 2005. She also identified reasons for the Finance Department's recommendation of Bank of America for commercial banking services approval of this item.
- BBT has also been contacted to provide emergency back-up services.
- A motion was made by Charlie Rivenbark and seconded by Earl Sheridan to approve the recommendation to award a contract to Bank of America for the City's commercial banking services for a term of five years. The motion carried.
- See Attachment A.
- This item will be prepared for consideration at the April 6, 2010 Council Meeting.

**3. Review for Approval – The recommendation to award a contract to McGladrey & Pullen for the City's Annual Independent Audit for the Fiscal Years ending June 30, 2010 through June 30, 2014.**

- Debra Mack reviewed the background and identified reasons for approval of this item.
- The City has been with the current firm, Lanier Whaley & Craft for 15 years.
- A fresh set of eyes with specialized testing of our areas will be good.
- The fee structure was also very attractive.
- A motion was made by Charlie Rivenbark and seconded by Earl Sheridan to approve the recommendation to award a contract to McGladrey & Pullen for the City's Annual Independent Audit for the Fiscal Years ending June 30, 2010 through June 30, 2014. The motion carried.
- See attachment B.
- This item will be prepared for consideration at the April 6, 2010 Council Meeting.

**Adjournment:**

The meeting was adjourned at 12:05 p.m.

**Next Meeting Date:**

Monday, May 17, 2010, in the City Manager's Conference Room, following the Agenda Briefing meeting.





# Memo

To: Audit Committee and Internal Auditor

Via: Sterling Cheatham, City Manager

From: Debra H. Mack, Finance Director and Bryon Dorey, Assistant Finance Director – Treasurer

Date: 3/17/2010

Re: **Proposals for Core Banking Services**

The City submitted a request for letter proposals for banking services to 12 banks with branches located inside the City limits. Each of these banks was identified by the Local Government Commission as operating under the State Treasurer pooling method of collateralization. The contractual period with the chosen firm will be for a five year period with optional extensions for up to 2 additional five year terms with mutual consent of both parties and City Council.

The seven firms responding to the proposal were Bank of America, RBC, SunTrust, First Bank, Wachovia, First Citizens and BB&T. Attached as Exhibit A is the analysis of each bank's level of non-compliance with the City's requirements. You will see that, as our bank service provider since 2005, Bank of America meets all of the City's requirements for core banking services. Over the last five years, the services received by the City have been tailored as needs have been identified. The remaining banks offer varying degrees of compliance with the City's requirements ranging from SunTrust with only 2 areas of non-compliance to RBC with over 10 areas of non-compliance or partial compliance.

Attached as Exhibit B is a net cost comparison developed from the banks' proposals for fees and interest rates. Proposed service charges based on historical transaction volumes are offset by estimated interest earnings on average account balances. The results are presented as estimated net interest earnings (cost) over the 5 year contract period. Given the unusual nature of the current interest rate market, the approach of this analysis is to compare the proposals over a range of interest rate environments. At the low end of the range are current interest rates and at the high end are 2008 rates. Interest rates in 2008, although higher than current rates, were still below "normal" and serve as a conservative estimate of where rates may go during the contract period. The analysis ranks the banks in increasing order of cost according to their average earnings (cost) across the range of interest rate environments. You will see from this analysis that the cost proposals from First Bank, Wachovia, First Citizens and BB&T contemplate significant cost increase to the City over the 5 year period. The cost proposals from Bank of America, RBC and SunTrust are closely aligned with that of Bank of America being the most cost advantageous.

Given the adverse financial impact of the proposals from First Bank, Wachovia, First Citizens and BB&T, the focus of our consideration is on Bank of America, RBC and SunTrust. As identified in Exhibit A, there are a number of areas where RBC does not meet the requirements of the City. The most significant of these is the inability to receive and process a payroll direct deposit file from the City one business day before the pay date. RBC requires receipt of the file 2

days prior to the pay date. Although the City's recent changes to the payroll schedule allows us to now routinely submit a file 2 days ahead, RBC would limit our flexibility in the event that any payroll issues arise. In addition, RBC does not yet offer payee positive pay which the City has learned is important to protect the City against fraudulent check cashing given the accessibility of software and printing technology to change the payee on a check.

Our analysis of SunTrust's proposal identified no significant area of non-compliance with City requirements that would preclude them from providing this service; however, it is important to note that SunTrust is the only bank in the group of respondents that does not have a presence in the downtown area.

#### Recommendation

Bank of America is currently meeting the City's core banking service requirements. Considering that no significant gains in functionality or anticipated cost savings were identified in the alternative proposals combined with the challenges of an approximately 4 month transition effort if banks are changed, we recommend that the City award the contract to Bank of America. We look forward to the opportunity on March 22<sup>nd</sup> to discuss these proposals.







	BOA	RBC	SunTrust	FirstBank	Wachovia	First Citizens	BB&T
12c On-line check & ACH return report							
12d On-line positive pay exceptions report							
Ability to accept or deny exceptions on-line							
Available by 10:00AM for previous day's exceptions							
13 Stop payment service - on-line request							
Stop payment service - verbal request							
On-line check status inquiry availability							
14 On-line access to paid check images							
How long after clearing is check image available?							
15 On-line wire entry							
On-line repetitive wire template availability					?		
On-line approval hierarchy availability					?		
16 On-line account transfer entry							
17 Direct deposit							
Can receive file by 11:00AM 1 business day before payday							
18 ACH debit availability		X				X	
19 On-line wire transfers							
Telephone backup wire transfers							
20 On-line wire templates							
Ability to restrict access & amount for specific users					?		
Ability to hardcode certain wire template sections					?		
21 Prenumbered/preencoded deposit slips for 23 locations					?		
In triplicate							
No charge					X		⊙
22 Endorsement stamps (2) - for each locations - no charge							⊙
23 Fee free checking accounts to City employees							
24 Free check cashing of City checks even if no account							⊙
25 Account reconciliation - paid item file							
Electronic monthly statement download							
26 ACH blocks on specific accounts							
ACH filters on specific accounts							
Notification of ACH block		X					
On-line access for ACH Filter status verification		X	X			X	?
27a Positive pay - transmission process							
27b Same day?		X	X				X
27c Applied at teller line?		X					
27d On-line manual issue?		⊙					⊙
27e On-line issue cancel?		⊙					⊙
27f Any volume limits on exceptions?							
27g Default disposition availability for exception items?		⊙					

	BOA	RBC	SunTrust	FirstBank	Wachovia	First Citizens	BB&T
27h Payee positive pay?				X		X	
28 Deposit exceptions forwarded to City next business day		X					
Detail support?							
29 Research assistance on transaction within 72 hours							
30 Provide large safe deposit box if needed							
31 Provide disposable night drop deposit bags at no charge		X					⊗
32 Process change orders as needed							
33 Payment of fees options - direct payment or draft							
34 Bank Statements within 10 business days following month							
35 CD-ROM monthly of paid items - with related software							
36 Monthly detail account analysis							
<b>General Information</b>							
* Credit Ratings				No Public Debt			
* Audited Financial Statements - 3 yrs							
* Explanation of interest bearing proposals							
* Past rates July-December 2008 / July-December 2009							
* Explanation of non-interest bearing proposals							
* List Branch locations in Wilmington							
* List 5 references of similar volume and complexity							
* Services provided by third parties		Wire System	Acct Recon				



## Exhibit B

### Analysis of Responses to Bank Services RFP

#### Estimated Net Interest Earnings (Cost) over 5 Year Contract Period

	Range of Net Earnings (Cost)		Average Estimated Net Earnings (Cost)	Range of Estimated Savings (Cost) to Change from Bank of America		Average Estimated Net Savings (Cost)
	At 2010 Market Rates	At 2008 Market Rates		At 2010 Market Rates	At 2008 Market Rates	
1 Bank of America	(62,493)	217,919	77,713			
2 RBC	(57,618)	211,130	76,756	4,875	(6,790)	(957)
3 SunTrust	(51,686)	202,958	75,636	10,807	(14,961)	(2,077)
4 First Bank	(78,709)	109,109	15,200	(16,216)	(108,810)	(62,513)
5 Wachovia	(164,319)	9,709	(77,305)	(101,826)	(208,210)	(155,018)
6 First Citizens	(202,815)	18,726	(92,045)	(140,322)	(199,194)	(169,758)
7 BB&T	(112,088)	N/A *	N/A *	(49,595)	N/A *	N/A *

Note:

Given the unusual nature of the current interest rate market, this analysis looks at the estimated net earnings (cost) resulting from each bank's proposal over a range of interest rate environments. At the low end are current interest rates and at the high end are 2008 rates. The 2008 interest rates, although higher than current rates, were still below "normal" and serve as a conservative estimate of where rates may go during the contract period.

\* BB&T did not provide their rates for 2008.





# Memo

To: Audit Committee and Internal Auditor

Via: Sterling Cheatham, City Manager

From: Debra H. Mack, Finance Director and Bryon Dorey, Assistant Finance Director – Treasurer

Date: 3/17/2010

Re: **Proposals for Auditing Services**

Attached are three proposals received for auditing services for the City's independent audit for the fiscal year ending June 30, 2010. Two local firms, Hardison, Chamberlain & Thomas PA and Goodson & Taylor CPA's declined to submit a proposal. The proposals also include fees for four additional years as requested in the RFP.

The three firms responding to the proposal were Lanier, Whaley, Craft and Co. CPA's (Lanier), McGladrey & Pullen LLP (McGladrey) and Thompson, Price, Scott, Adams & Co. PA (Thompson). Lanier has one office located in Wilmington, with 13 professionals, including 3 partners. They are proposing that Charles Craft continue to be the engagement partner as he has in the past 15 years with the City. McGladrey & Pullen LLP is a national firm that operates in an alternative practice structure with RSM McGladrey. The companies have 90 offices nationwide with some 7,500 employees, of which 700 are partners. In North Carolina, McGladrey has eight offices with 375 employees, of which 31 are partners. The staff for the audit would be drawn from their Wilmington office and other North Carolina offices. The engagement partner would be Lou Cannon from their New Bern office. Thompson has an office in Wilmington, Elizabethtown and Whiteville with an unspecified total number of professionals of which 3 partners and 5 staff would be involved in the engagement. It is not specifically addressed as to which partner would be the engagement partner although Alan W. Thompson is listed first among the partners to be involved in the engagement.

## McGladrey & Pullen LLP

As you will see from the proposals, the McGladrey firm is more detailed in their description of their audit approach. They have standard audit programs which they have designed for their many municipal clients which will be tailored to the needs of the City. In Section II of their proposal (pages 2-3) they describe their risk assessment approach to identify the nature and extent of substantive testing they will perform including utilization of statistical sampling. They do have resources on a regional and national level that can be called upon to provide technical assistance in many areas of local government finance. On page 4 of Section II a description of the engagement team is given with approximate time each member will be committed to the audit. On page 8 of Section II a detail of hours for the engagement are given. They anticipate 748 total hours with the engagement partner providing approximately 6% or 48 hours. The on-site in-charge will provide 198 hours or 26% of the engagement hours. Pending review of the complexity of the City's computer accounting system and related controls, a computer audit specialist may be utilized to prepare and review the systems documentation. Among McGladrey's many municipal clients are New Hanover County, the Cape Fear Public Utility



Authority, City of Jacksonville, City of Durham and City of Greenville. McGladrey performed the City of Wilmington audit from 1992-1994.

#### Lanier, Whaley, Craft and Co. CPA's

Lanier's proposal is for an audit approach designed specifically for the City engagement. Their proposal (Section II, page 1) does not provide a detailed approach but indicates that their reliance on substantive testing (test of details) is an integral part of their audit program. Their proposal (Section II, page 4) calls for a total of 1,000 hours with the engagement partner and other partners providing 100 hours or approximately 10% of the hours. The on-site managers (seniors) of the engagement would contribute 300 hours or 30% of the total hours. Use of a computer audit specialist is not anticipated. In addition to 15 years of experience auditing the City, Lanier provides audit services to other governmental entities including the Cape Fear Public Transportation Authority and the New Hanover County Airport Authority.

#### Thompson, Price, Scott, Adams & Co. PA

Thompson's proposal is to utilize standard PPC audit programs that will be tailored specifically for the City engagement. Their proposal does not provide detail about the audit approach except that statistical sampling will be utilized for tests of compliance, tests of internal control and disbursement testing (page 2 of Section II). Their proposal (Section II, page 4) calls for a total of 688 hours with the engagement partner and other partners providing 200 hours or approximately 29% of the hours. The on-site managers (seniors) of the engagement would contribute 312 hours or 45% of the total hours. Use of a computer audit specialist is not anticipated. Thompson provides audit services to other governmental clients including Johnston County, Pender County, Columbus County and several towns with population less than 10,000. With the exception of Johnston County, these audit service recipients are not of comparable size to the City.

#### Fee Proposals

The fee proposal for McGladrey is for \$68,820 the first year with a 1% to 1.4% increase the next 3 years and no increase the last year. The total would be \$351,820 for the five-year period. The fee proposal for Lanier is \$89,500 the first year with a 3% increase for each of the next four years. The total would be \$475,000 for the five-year period. The fee proposal for Thompson is for \$69,960 for the first year with no increase for the next four years. The total would be \$349,800. While the fee proposals for McGladrey and Thompson are in close proximity, the Lanier proposal is \$123,180 and \$125,200 or 35% higher over the five-year period than the other two proposals. However, in terms of average hourly rates, the Lanier proposal is approximately \$95, the McGladrey proposal is \$94 and the Thompson proposal is \$102.

#### Other Concerns and Considerations

McGladrey's audit program is more computer driven and they bring experts from many disciplines to the engagement. Lanier relies more heavily on detailed testing and more hands-on involvement from the audit partner and manager that results in more fieldwork hours but also provides flexibility in hours allocated to the job if the firm has to wait on schedules or other information from staff. The Finance staff must continue to provide support for the fiscal operations of the City while the audit is underway. Both of these firms are well qualified to provide the City of Wilmington quality auditing services. Thompson's apparent focus on municipalities of significantly smaller size than the City combined with limited disclosure regarding audit approach and lack of previous experience with the City makes their proposal the least attractive of the three.



### Recommendation

We recommend that the Committee consider awarding the audit contract to McGladrey. Given that Lanier has audited the City's financial statements for the past 15 years combined with the opportunity for significant cost savings to the City, changing from Lanier seems a prudent consideration. Although, Thompson's record of experience tends to favor smaller municipalities, McGladrey brings experience auditing municipal clients of comparable size in addition to prior experience auditing the City.

We look forward to the opportunity on March 22<sup>nd</sup> to discuss these proposals. If the members wish to interview the firms we will make the appropriate arrangements fitting with your schedules.